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BEFORE THE
SURFACE TRANSPORTATION BOARD

COMPETITION IN THE RAILROAD INDUSTRY

STB Docket No. EP 705

THE MERCURY GROUP
A Shipper-Based Mobile Energy Study Group

TESTIMONY OF CRAIG S. DICKMAN ON BEHALF OF THE MERCURY GROUP

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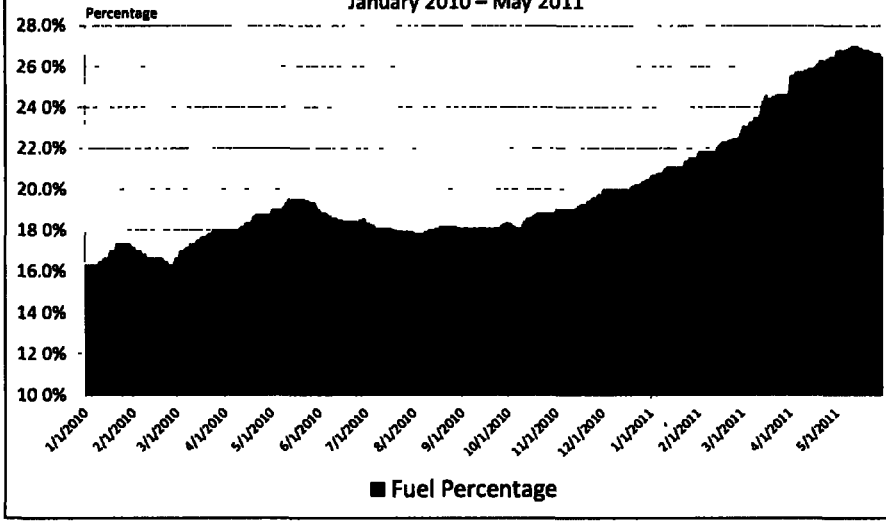
Chairman Elliott, Vice Chair Begeman, Commissioner Mulvey, staff and interested parties; my name is Craig Dickman, and I would like to thank you for the opportunity to appear before you today.

Today I am appearing on behalf of The Mercury Group, a shipper group focused on understanding the energy component of freight movements.[1] As such, my perspective is from the shipper point-of-view and how they can effectively manage the energy used in the movement of their goods. This is critical to a shipper because, as Chart 1 indicates for the period from January 2010 forward, for example, fuel has averaged more than 20% of the total intermodal cost of moving their goods to market.

CHART 1
INTERMODAL FUEL AS A PERCENTAGE OF TOTAL FREIGHT
January 2010 – May 2011



With the significance of fuel costs to their overall intermodal freight costs, it only makes sense that shippers will want to both understand these costs and use this information to make better decisions about how to move their goods. The challenge, however, is that the current competitive marketplace makes it virtually impossible for shippers to understand the fuel consumption, fuel costs or energy-related emissions that are a critical component in effectively moving their goods to market.

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[1] Initial Comments of The Mercury Group are filed herein, dated April 8, 2011.

And it is our belief that any discussion of an efficient, competitive marketplace must include a thorough review and understanding of the 20% of total freight costs that are incurred by mobile energy. If the marketplace can be transformed, as we believe it can, to provide market participants such an understanding of the energy component of the transportation, we believe the result will be that rail and rail intermodal movements will become more competitive, leading to conversion of more freight and more diverse movements to rail.

As part of the Mercury Group – which more specifically is a shipper-based fuel study group – we lead a study to understand the current fuel surcharge environment and how well it reflected actual fuel price behavior in the marketplace. Our study included multiple shippers, across multiple industries, multiple intermodal marketing companies, and the four principal Class I railroads, and an assessment of 184,674 unique intermodal freight movements over the period of one year. This sample set included only movements between 1000 and 2000 miles and only movements that could be served with standard size, dry-freight containers.[2]

We would like to share some of our data and findings with you today.

First, Chart 2 highlights the fuel market price behavior from January 2010 through May 2011. The chart highlights the price behavior of three energy benchmarks:

- DOE On-Highway Diesel. This is the national average price for diesel fuel that is published weekly by the DOE and is used frequently as the key price measure in intermodal fuel surcharge programs.
- Diesel Market Price. This is the average daily price for diesel fuel – at truck stops across the country – that reflects a typical purchase price in the market. You may ask why we use on-highway prices as a benchmark. Simply, with the DOE Index being a proxy for many intermodal fuel surcharge programs, we look to compare how accurately that price reflects the underlying diesel fuel marketplace.
- WTI Crude Oil. This is the daily spot price for crude oil and is reflected on the secondary axis in dollars-per-barrel.

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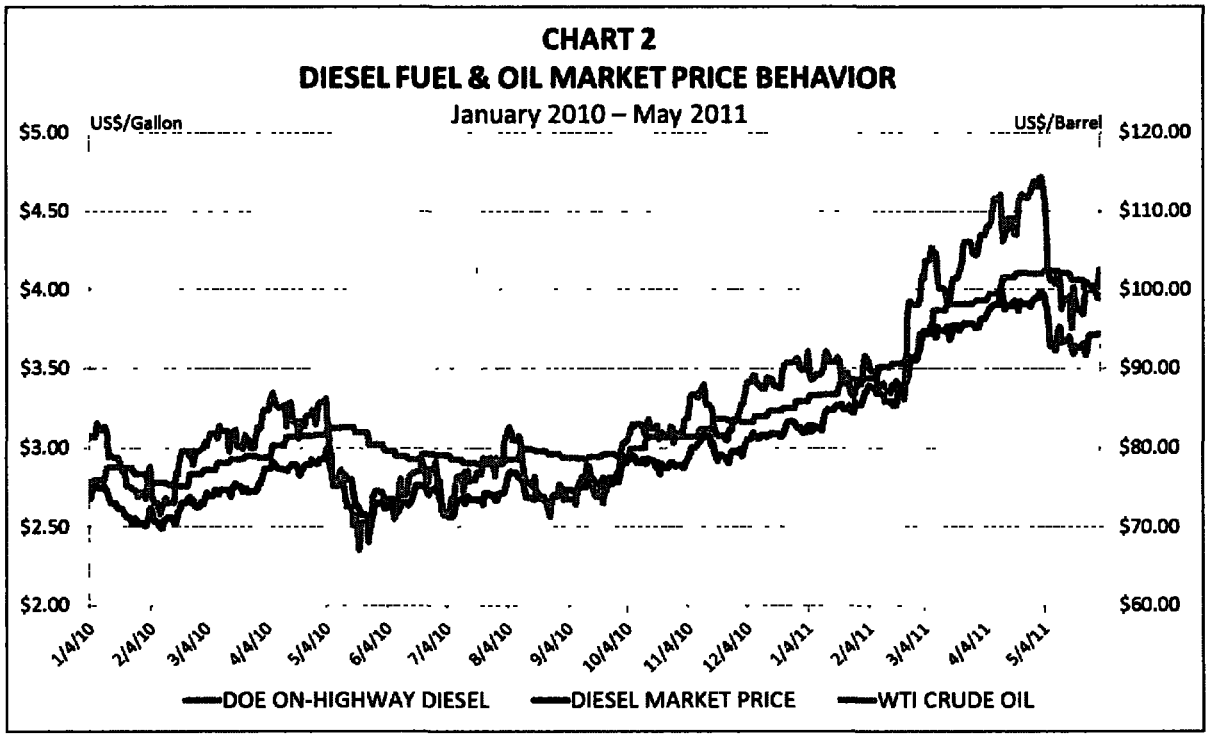
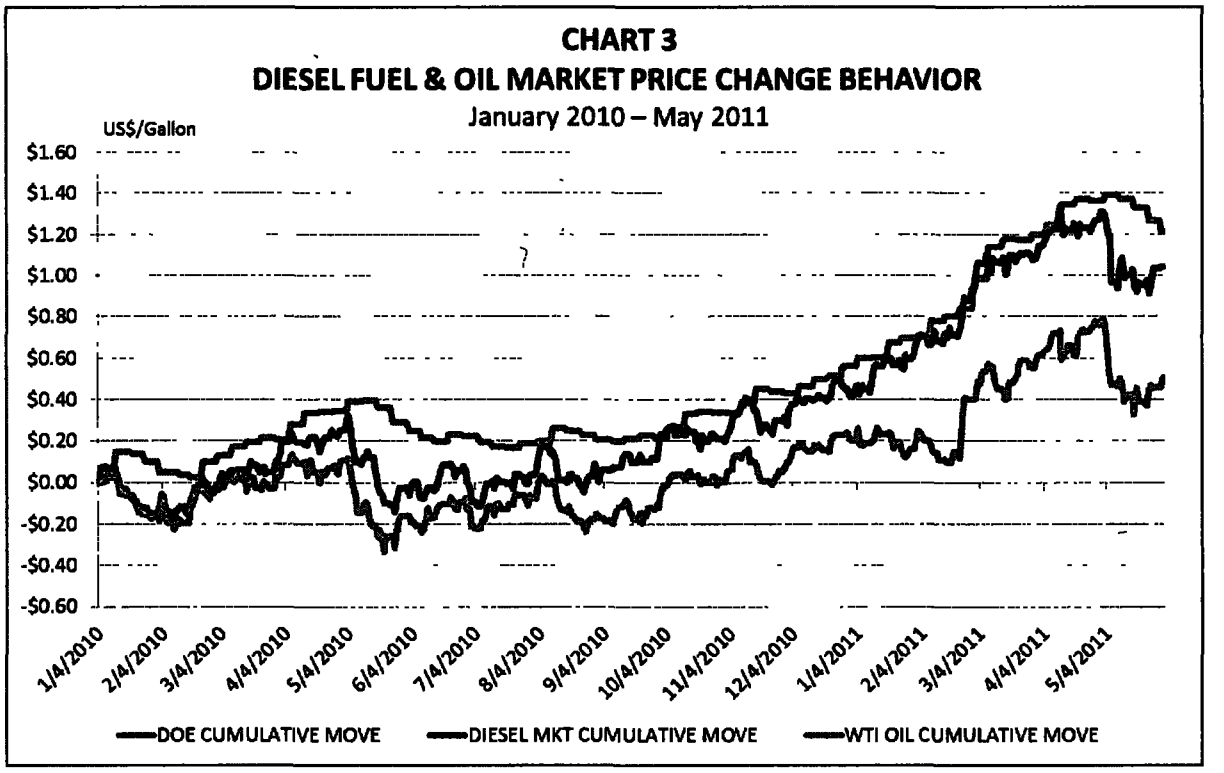
[2] The Mercury Group Initial Comments, pp. 20-27.

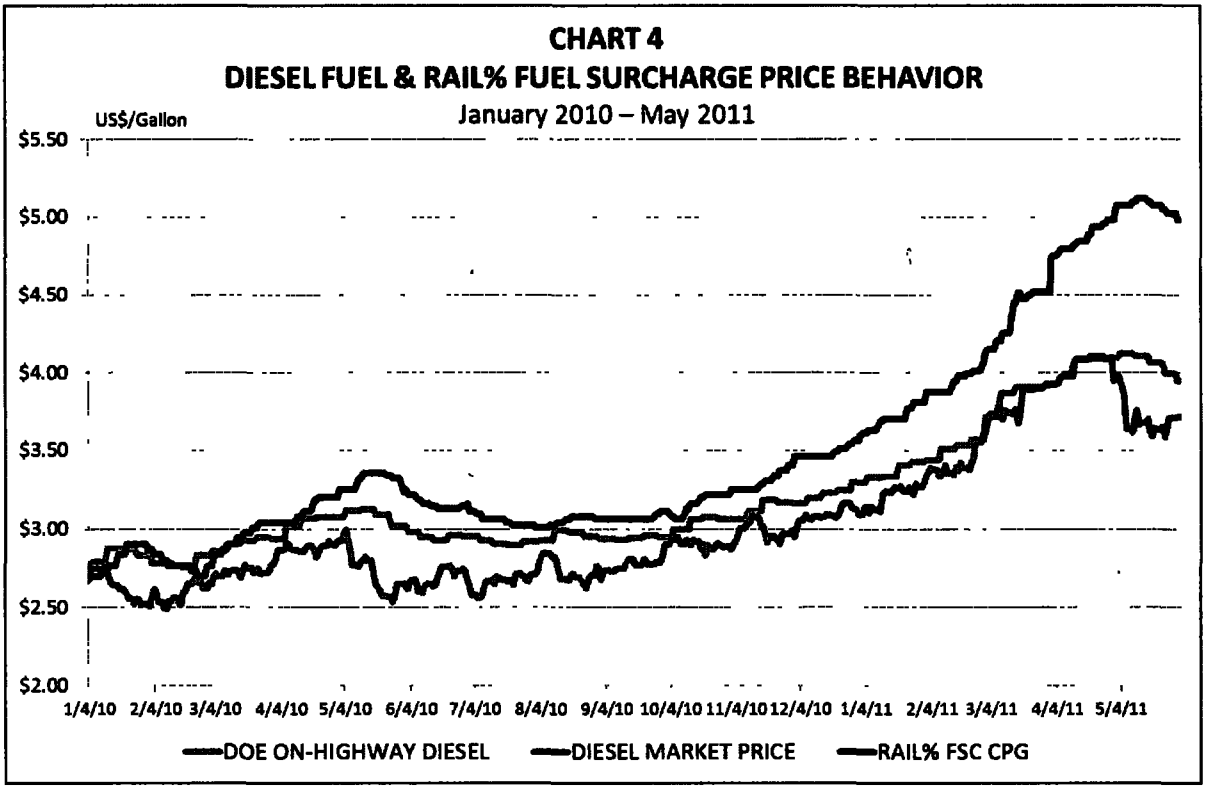
As you can immediately see, each of these benchmarks has slightly different characteristics. The DOE index both mutes the daily price changes and misses select market movements. The crude oil benchmark indicates the underlying behavior of diesel's raw material but is influenced by different supply/demand characteristics and, as a result, does not always align with diesel price movements. It should be noted, here, that the Diesel Market Price reflects prices most closely aligned with what trucks pay for fuel and, after they are adjusted for tax differences between truck and rail, shows the price movement that railroads are exposed to.



As we expand on that point – the daily price movements that impact rail and truck providers – we present Chart 3. This chart starts with the first business day of January 2010 and extends the price moves through the end of May 2011. We believe this helps build an understanding of the price behavior and, you will see, sets a foundation for comparison for intermodal-based fuel surcharges.



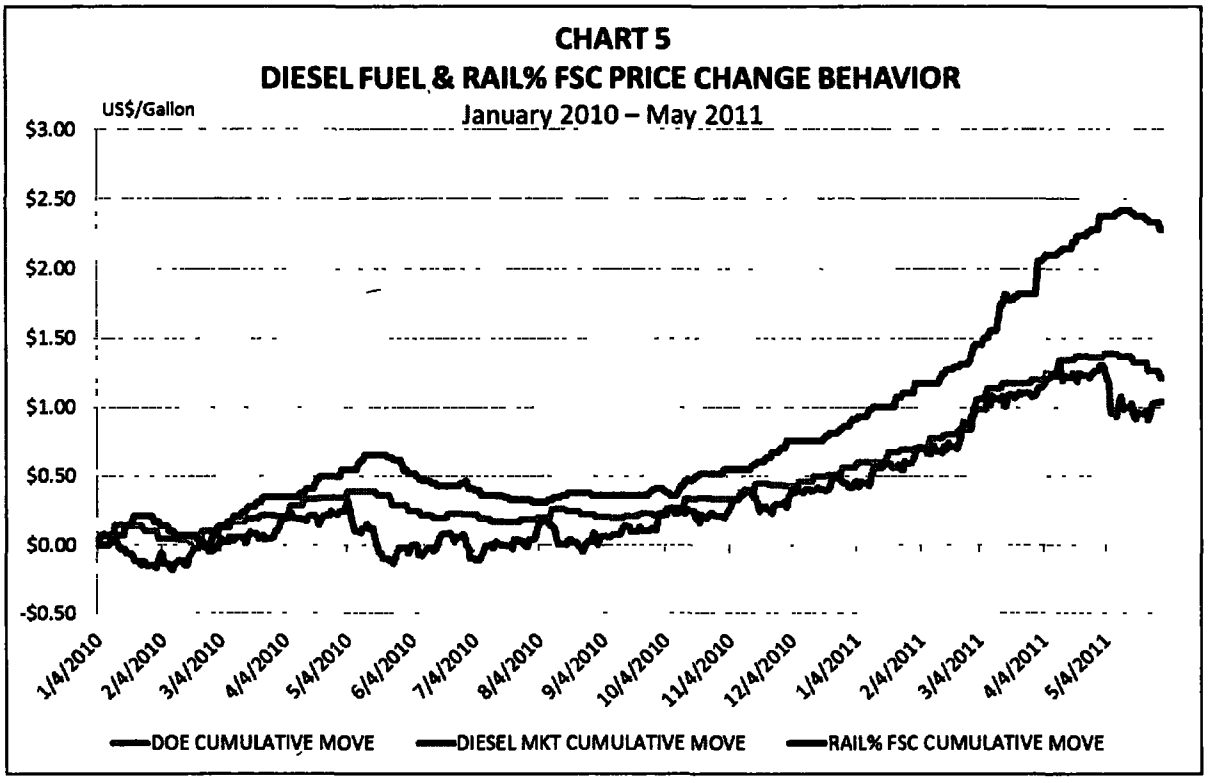
Our study now shifts from an understanding of fuel behavior to how the intermodal fuel surcharges are applied to real freight movements. Our study of the more than 184,000 freight movements isolated the fuel costs and, using rail industry standards, converted the surcharges back to a cost-per-gallon impact. Chart 4 highlights the results of this analysis and compares the intermodal fuel surcharges – based on a percentage of revenue method – with the diesel price behavior we reviewed in the prior slides.



We then present this data, in Chart 5, to show the daily price movements that have occurred since January 2011. We believe this data provides a few observations:

- First, the general relationship between the fuel surcharge prices and the DOE index becomes apparent. The issue we referenced earlier – of the DOE muting and missing some of the price movements – is embedded in the rail fuel surcharge price behavior.
- Also, it becomes apparent that the rail fuel surcharge method exaggerates the behavior and lags the behavior of the DOE index. Increases are extended much greater than the actual market movement. While this 17-month period has not provided for significant price decreases, what we see is that declining markets will be exaggerated as well. As a result of this exaggerated

behavior – in both directions – we see that every movement artificially benefits either the transportation provider or the shipper.



This highlights a couple of the key challenges we see with the current fuel surcharge method:

1. Because of the exaggerated behavior – when compared to the actual fuel marketplace – we find that there is a winner and loser in virtually every fuel transaction. This does not set-up for a healthy relationship between the shipper and carrier when it comes to fuel programs.
2. The fact that fuel surcharges are somewhat detached from the underlying market creates significant challenges for the shipper:
    a. Budgeting becomes difficult. Shippers may budget an underlying fuel cost but they likely have no visibility to the exaggerated fuel surcharge behavior and could hit their plan price and still be way off budget.
    b. Making mode decisions becomes difficult. The fuel price behavior – and the behavioral differences between truck and rail fuel prices – can change the total cost relationship between modes and can affect the shipper's decision making process.
    c. Even hedging becomes difficult. This price distortion creates real problems with risk management. If the intermodal fuel surcharges do not align with fuel market

behavior, the problem extends to the products – such as heating oil or crude oil – that are frequently used for hedges. In fact, we have heard from members who thought they had hedges in place, only to find that their prices increased but the hedges did not move in concert and they were left exposed – even though they placed hedges on their fuel uses.

It is our belief that the analysis indicates that the current industry accepted methodology for fuel surcharges is inefficient and does support an open and competitive marketplace.

At the same time, we believe the opportunity to move toward a more competitive marketplace exists today. To do so, we believe it is necessary to provide:

- Energy lifecycle transparency. A common and accurate view of fuel costs (price and consumption) related to freight movements. This enables effective decision-making.
- An accurate reflection of actual prices and price movements. This builds trust between the shipper and carrier.
- Alignment between the fuel market and the reimbursement provided to transportation providers. This will enable the decisions made to produce the economic impact anticipated by the decision. These decisions can include the choice between using truck or rail for a shipper's freight movement.

Further, we believe the result will be that rail and rail intermodal movements will become more competitive and – when we have seen these principles applied – leads to conversion of more freight and more diverse movements to rail.

We also believe it is unlikely that this shift will occur organically. Rather, we believe that it will take clear and decisive public policy to move the industry toward a more open and transparent fuel management approach. And we realize that the change to this more competitive market will not be without challenges or detractors. But, we believe the benefits are significant and well worth the effort.

We also believe The Mercury Group is in a unique position to support the analysis and understanding of fuel programs. If the Surface Transportation Board institutes an investigation or, better, facilitates a process and a forum for discussions to improve the state of fuel management with the goal of enhancing

rail competitiveness, The Mercury Group and its members will participate fully. It is our ultimate hope that the STB will pursue a collaborative process for shippers, including Mercury Group members, the railroad, and industry interests to explore how to bring transparency of fuel costs to the rail and intermodal industry and, thus, create a more effective, competitive marketplace.

Thank you for the opportunity to present this testimony today.

Breakthrough Fuel

Intermodal Fuel Market Behavior

CHART 1
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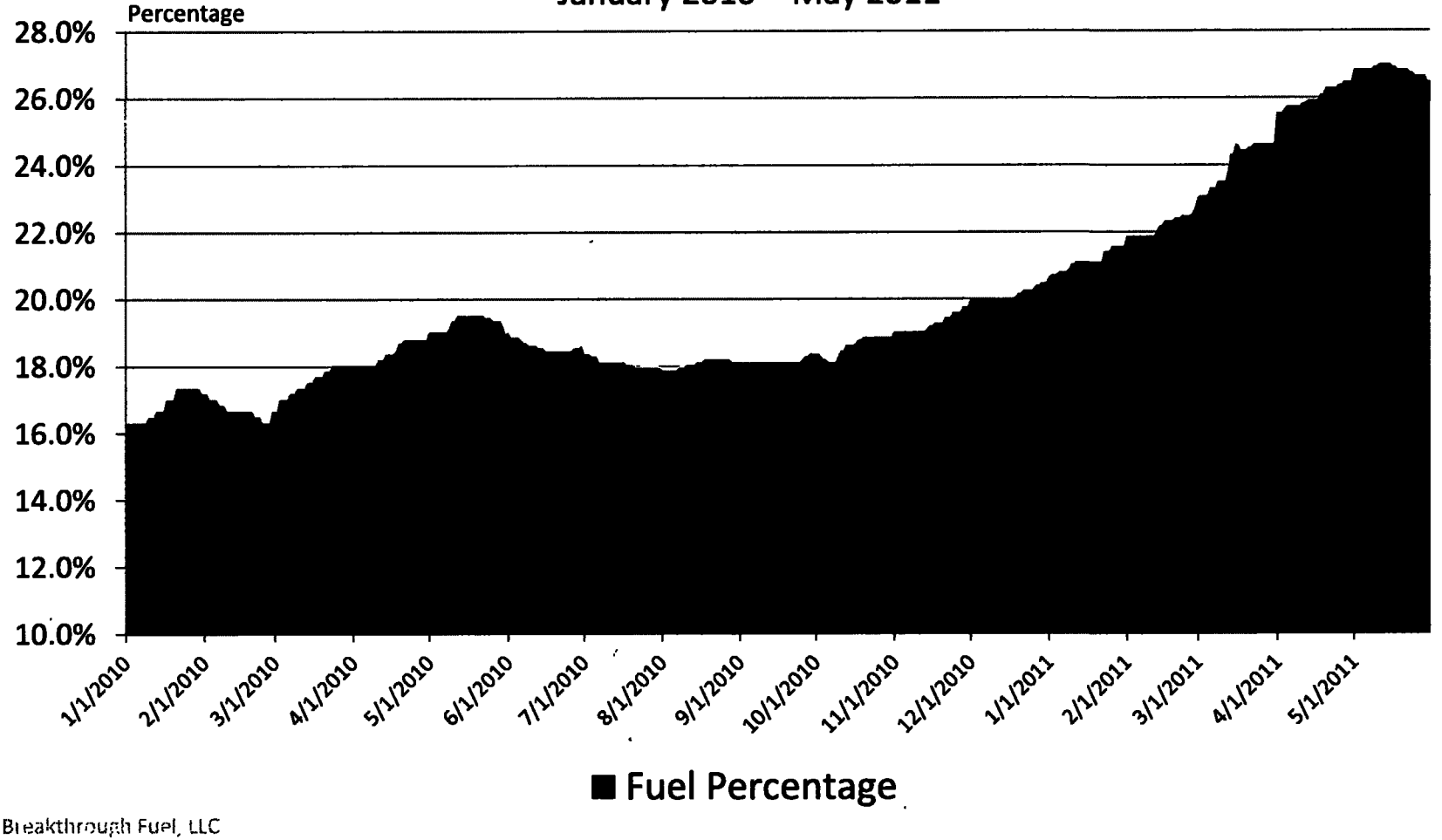
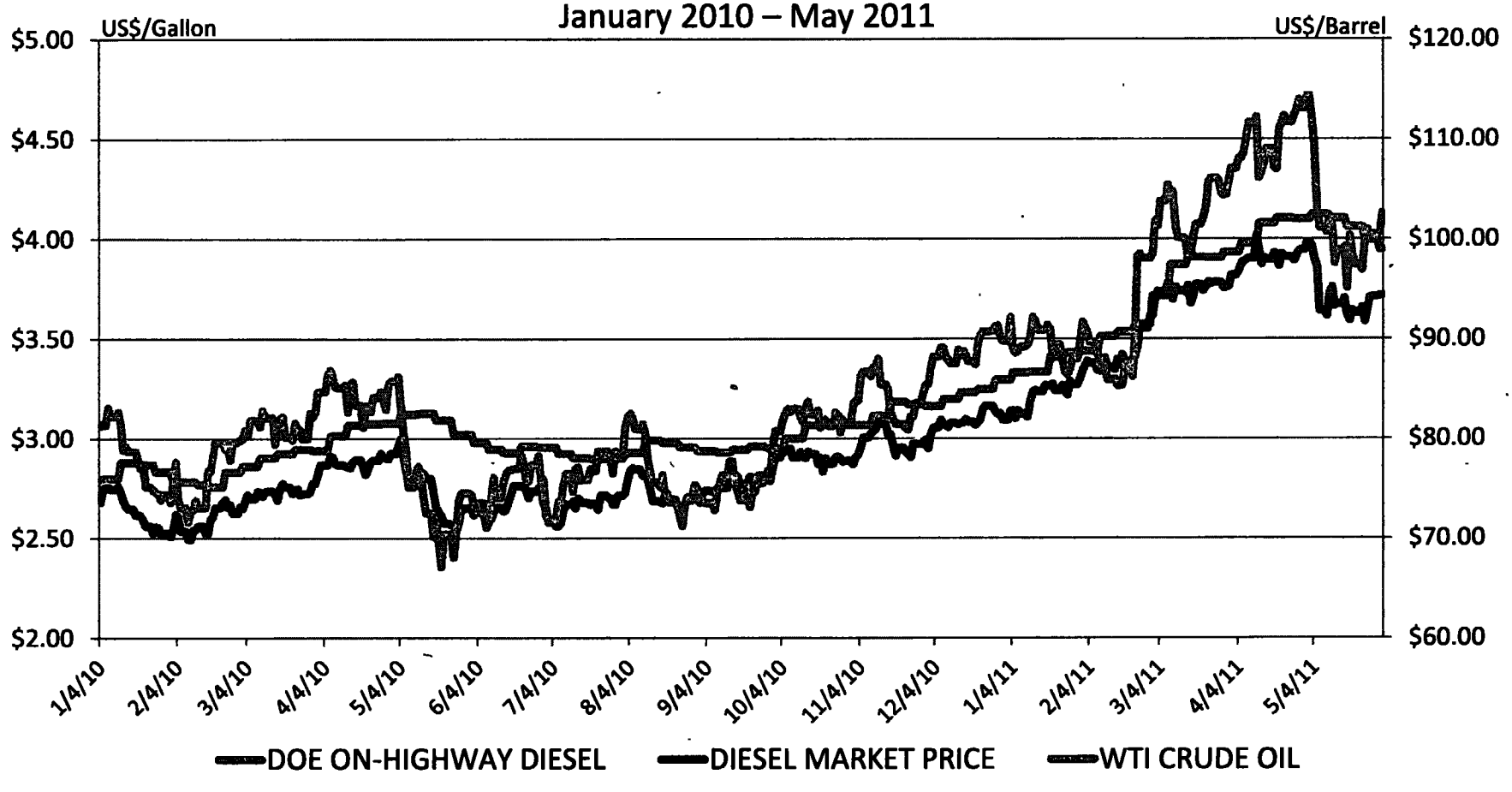
January 2010 – May 2011



Breakthrough Fuel

Intermodal Fuel Market Behavior

CHART 2
DIESEL FUEL & OIL MARKET PRICE BEHAVIOR
January 2010 – May 2011



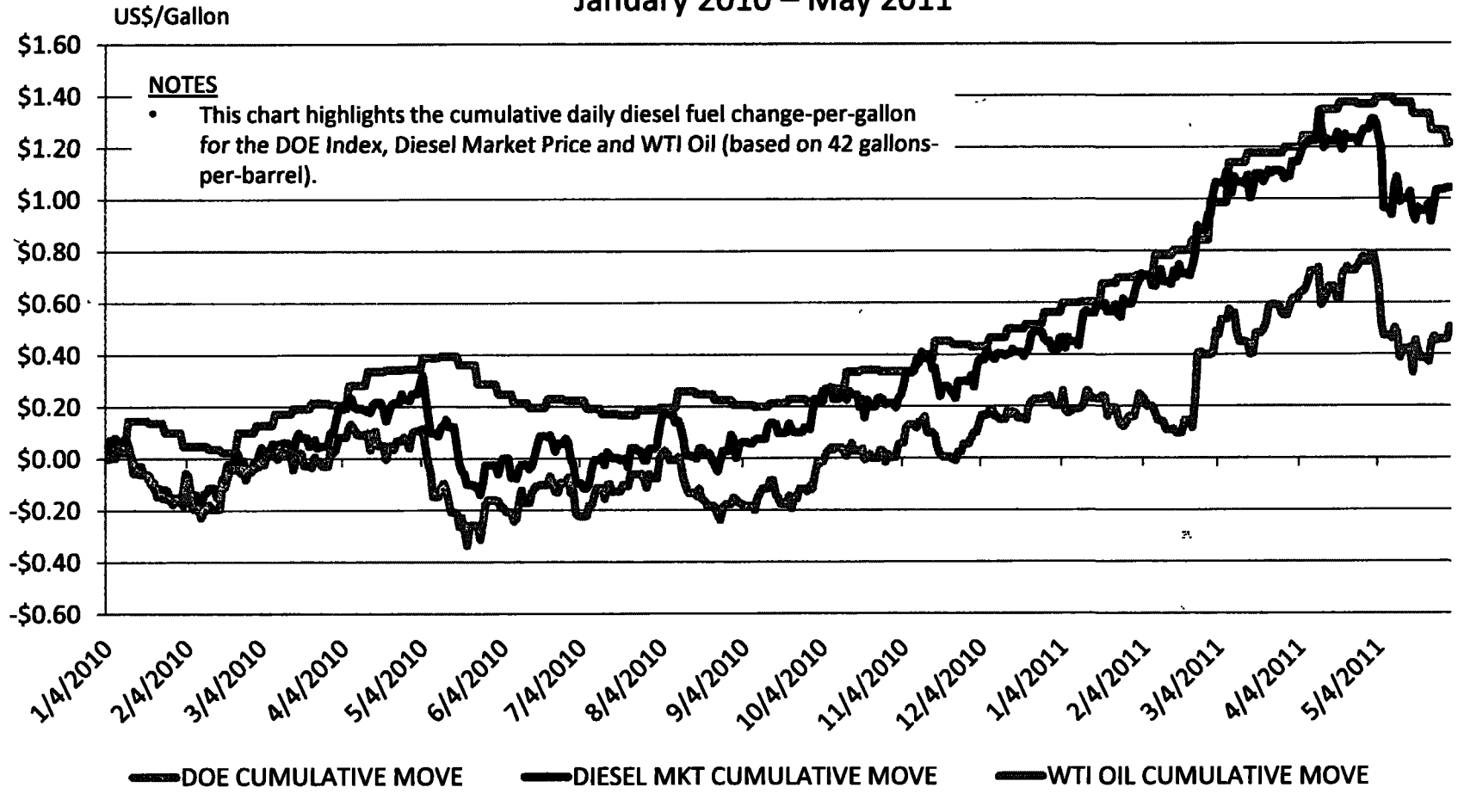
Breakthrough Fuel

Intermodal Fuel Market Behavior

CHART 3

DIESEL FUEL & OIL MARKET PRICE CHANGE BEHAVIOR

January 2010 – May 2011



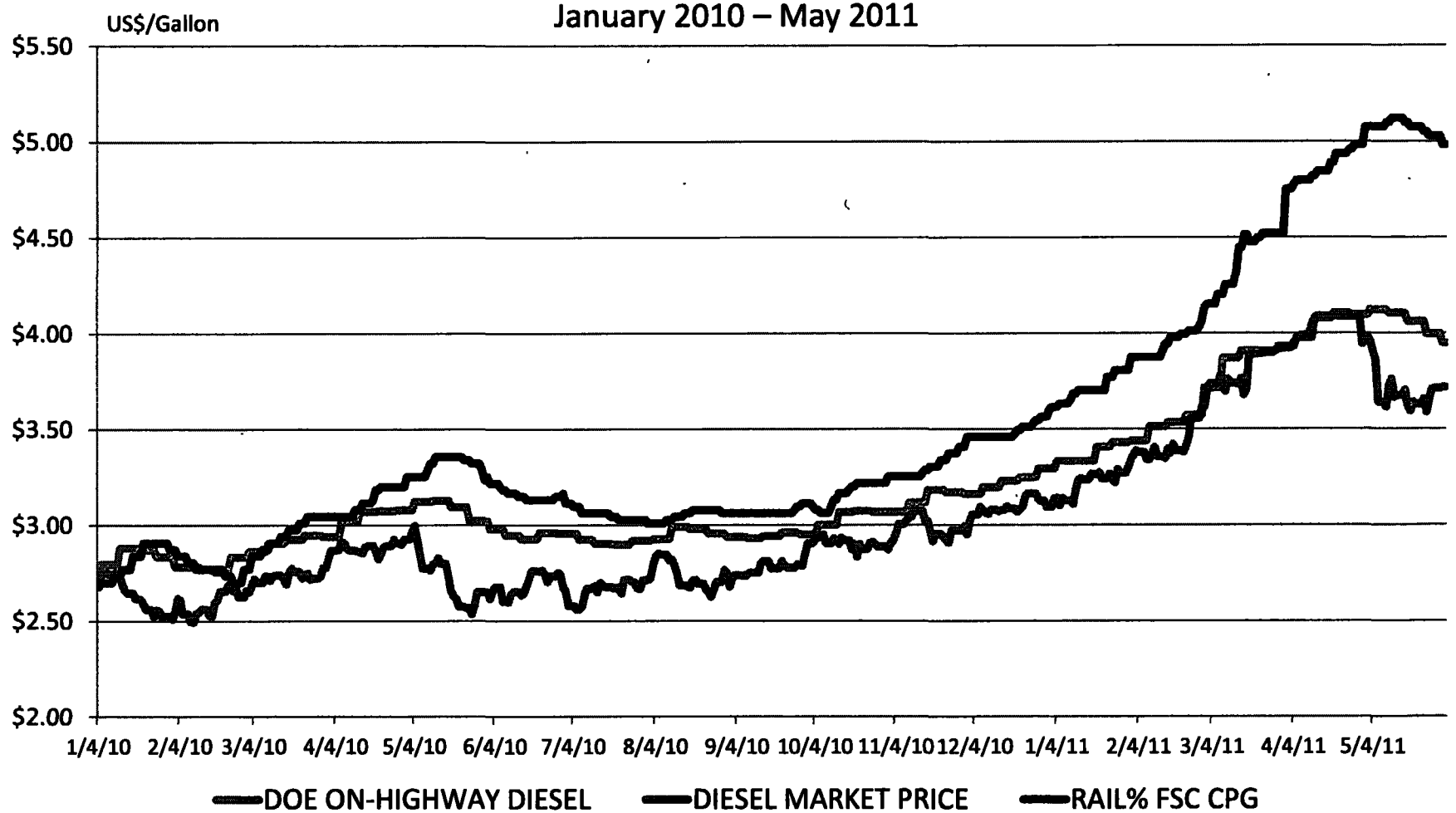
Breakthrough Fuel

Intermodal Fuel Market Behavior

CHART 4

DIESEL FUEL & RAIL% FUEL SURCHARGE PRICE BEHAVIOR

January 2010 – May 2011



Breakthrough Fuel

Intermodal Fuel Market Behavior

CHART 5

DIESEL FUEL & RAIL% FSC PRICE CHANGE BEHAVIOR

January 2010 – May 2011